IN THE

Supreme Court of the United States

October Term, 1977

No. 77-305

DORIS M. BAUER, LOU ANN MURPHY and BRUCE G. MURPHY,

Petitioners,

v.

THOMAS W. GILLIAM, JR., ERIE COCKE, JR., and MADELYN GROTNES COCKE,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

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Counsel for Petitioner

TABLE OF CONTENTS

AUTHORITIES CITED

Doris M. Bauer, Lou Ann Murphy and Bruce G. Murphy pray that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals for the Fourth Circuit entered in the above case on February 22, 1977, rehearing denied on May 25, 1977.

OPINIONS BELOW

In the district court, on January 31, 1976, the jury returned verdicts in favor of each of the defendants against each of the plaintiffs. The unpublished opinion of the court of appeals together with its order changing paragraph two of page 4, is appended to this petition.

JURISDICTION

The judgment of the court of appeals was entered on February 22, 1977, rehearing denied on May 25, 1977.

The jurisdiction of this Court rests on 28 U.S.C. §1254 (1) (1966).

QUESTIONS PRESENTED

1. Whether the district court erred in instructing the jury that "scienter" was necessary in an action under 15 U.S.C. §77 q (a).

2. Whether the district court erred in refusing plaintiff petitioners' requested instruction that reliance was not necessary in an action under 15 U.S.C. §77 q (a) nor under 15 U.S.C. §78 j (b) and instructing the jury instead that in both instances the defendant could show non-reliance.

STATUTES INVOLVED

1. Section 17(a), 15 U.S.C. §77 q (a) provides in part:

It shall be unlawful for any person in the offer or sale of any securities... directly or indirectly--

(1) to employ any device, scheme or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

2. Section 10(b), 15 U.S.C. §78 j (b), provides in part:

It shall be unlawful for any person ...

(b) to use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not

so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

RULE INVOLVED

Rule 10 b-5, 17 C.F.R. 240.

10 b-5 provides in part:

It shall be unlawful for any person ...

(a) to employ any device, scheme, or artifice to defraud,

(b) to make any untrue statement of a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) to engage in any act, practice

or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

STATEMENT OF THE CASE

The suit arises out of the investments by the petitioners in what has now become known as the "Great Wine Scheme" which was created by one Robert Dale Johnson. The respondent, Cocke, and Gilliam did business in the District of Columbia under the name of Cogill Partners.

Johnson accepted funds from various investors for the stated purpose of purchasing industrial wine in Europe for import to the United States and gave in return non-interest bearing promissory notes due in six to nine months from the date thereof and agreements to pay part of the profits in a guaranteed

minimum amount. No registration statement was filed with the Securities and Exchange Commission with regard to such transactions. No wine was ever in fact purchased by Johnson and the entire operation by Johnson was a fraud.

Johnson told the respondents that industrial wine purchases from Portugal did not have sufficient alcohol content to become entangled with alcoholic beverage laws and regulations and that the purchases were in conjunction or cooperation with the Government's AID Program through the Department of Commerce; that industrial wine was used in all types of salad dressings; that he had options to purchase industrial wine on a continuing basis in Europe in general and Portugal in particular; that he and his partners in the United States had developed

both United States and world wide markets for this product; that shipments were insured by Lloyd's of London; and that he had approached the stage of "cornering the market". He thereafter stated that the Government AID Program had ceased and that he and others comprising a group of five or six importers had divided up the country by territories to continue the wine import business and that the additional amount of promised return was the result of extra quality wine and the fact that a large amount of this wine was being shipped to Philadelphia and almost immediately trans-shipped to Japan.

All of the statements contained in the preceding paragraph were false, were communicated by the respondents to Frank E. Mower, II, and by Mower to the petitioners.

On January 8, 1975, petitioner, Bruce G. Murphy transferred $50,000.00 to Mower. On the same day, Mower combined Murphy's $50,000.00, together with monies of his own and other investors, and transferred to the respondents the sum of $170,000.00. Subsequently, Mower received Johnson's note dated January 9, 1974, in the amount of $170,000.00, payable to Cocke and endorsed to Mower, together with Gilliam's letter guaranteeing an investment return of $76,500.00. Cocke had a secret written agreement dated January 9, 1974, with Johnson guaranteeing an investment return of $110,500.00.

On February 11, 1975, petitioner Doris M. Bauer transferred $15,000.00 to Mower, and petitioner Lou Ann Murphy transferred $7,500.00 to Mower. On the same day, Mower combined these sums,

together with monies of other investors, and transferred to the respondents the sum of $100,000.00. Subsequently, Mower received Johnson's note dated February 14, 1974, in the amount of $100,000.00, payable to Cogill, and endorsed to Mower, together with Gilliam's letter guaranteeing an investment return of $45,000.00. Cocke had a secret written agreement dated February 14, 1974 with Johnson guaranteeing an investment return of $56,000.00.

Petitioners never recovered their investments or any returns on their investments. Suit for recovery was brought in the United States District Court for the Eastern District of Virginia, Norfolk Division. Jurisdiction was based on §22 of the Securities Act of 1933 and §27 of the Securities Exchange Act of 1934.

In the district court, petitioners alleged violations of Federal securities' laws and introduced evidence in support of their allegations. The district court held as a matter of law that the notes given by Johnson for the $100,000.00 and the $170,000.00 were securities within the laws of the United States and that the securities laws would apply.

Petitioners requested the district court to instruct the jury that "scienter" was not a necessary element in a §17(a) action. The district court also refused petitioners' requested instruction that reliance was not necessary in a §17(a) action and instructed the jury that the defendants could prove non-reliance.

Similarly, the district court refused petitioners' proposed instruction that reliance was not

necessary in a §10(b) action and instead instructed the jury that defendants could prove non-reliance.

A verdict was returned in favor of the defendants. On appeal, the court of appeals found that based on the "truncated transcript before us we cannot find that there was prejudicial error in the instructions here."

REASONS FOR GRANTING THE WRIT

This case presents two important questions of federal law which have not been directly confronted by the Supreme Court. First, is "scienter" a necessary element in a §17 (a) action? Second, is reliance a necessary element in a §17 (a) or a §10 (b) action? These questions should be resolved to insure uniformity of decision throughout the Circuits.

In Ernst & Ernst v. Hochfelder,

et al., 425 U.S. 185 (1976), the Court settled much uncertainty among the circuits as to whether "scienter" was a necessary element in a §10 (b) or Rule 10 b-5 action. The uncertainty regarding the "scienter" requirement in a §17 (a) action should also be resolved.

Certain Federal court decisions have already indicated that "scienter" may be required in a private action under §17 (a). See, e.g., Globus v. Law Research, Inc., 418 F.2d 1276 (2nd Cir. 1969); Odette v. Shearson, Hammill & Co., Inc., 394 F.Supp. 946 (S.D. N.Y. 1975). This requirement would seem to run counter to the Court's application of "scienter" in a §10 (b) action for two reasons. First, in Ernst & Ernst, supra, the Court placed considerable emphasis on the statutory wording of §10 (b); specifically

"manipulative", "device", and "contrivance" were mentioned. Such words are noticeably missing from §17 (a). Second, in Ernst & Ernst, supra, the Court noted that the language of Rule 10 b-5 could be used as proscribing certain wrongdoing whether intentional or not; however, it was necessary to read Rule 10 b-5 in conjunction with §10 (b), which restricted its application to intentional wrongdoing. The language of §17 (a) is very similar to that of Rule 10 b-5. It would seem, therefore, that §17 (a) should apply to both intentional or negligent wrongdoing.

In Affiliated Ute Citizens of Utah v. U.S., 406 U.S. 128 (1972), the Court appeared to provide a guide in applying the element of reliance in a §10 (b) action.

Instead, the Court has left unclear "to what extent reliance is

still an element in 10 b-5 actions." Note, The Reliance Requirement in Private Actions Under S.E.C. Rule 10 b-5, 88 Harv.L.Rev. 584 (1975), quoting Reeder v. Mastercraft Electronics Corp., 363 F.Supp. 574 (S.D. N.Y. 1973).

As a result the circuits are left to wrestle with the possibility of some presumption of reliance in §10 (b) actions. In addition, they are faced with the difficult question of whether such a presumption can be rebutted. The Third Circuit has said that a defendant in a §10 (b) action is permitted to show non-reliance. Thomas v. Duralite Co., Inc., 524 F2d 577 (3d Cir. 1975); Rochez Bros., Inc. v. Rhodes, 491 F.2d 402 (3d Cir. 1974). This, in effect, is the same as saying that the element of reliance is a necessary element in a §10 (b) action.

The Third Circuit, in Thomas v.

Duralite Co., Inc., supra, spoke of an "interplay between materiality and reliance which tends to blur the distinction between them when the factual backdrop changes." The Court, in order to avoid confusion and to insure uniformity among the circuits on the question of reliance in §10 (b) actions, should more clearly address and define this interplay and distinction. Otherwise, the circuits are left with the delicate task of balancing the subjective nature of materiality with the objective nature of investor reliance.

For similar reasons, the Court should address the problem of applicability of reliance in §17 (a) actions.

CONCLUSION

It is submitted that "scienter" was not intended to be a necessary element in a §17 (a) action. The Court's reasoning in Ernst & Ernst seems to support this contention. Certain Federal court decisions, however, indicate that "scienter" is a necessary element. Such a requirement would violate legislative intent and take away from the investor a very important statutory shield. Thus, it is important that the Supreme Court grant certiorari in this case.

It is further submitted that reliance is not a necessary element in a §10 (b) or §17 (a) action. Since the Court's decision in Affiliated Ute Citizens of Utah v. U.S., supra, the circuits have been unable to establish any set criteria for determining when

and to what extent reliance should be considered in a §10 (b) action. The Court should provide a more complete and uniform guideline upon which the circuits can base their decisions pertaining to the applicability of the element of reliance to §10 (b) actions.

For similar reasons, the Court should provide guidelines for the applicability of reliance in §17 (a) actions.

For these and the other reasons stated, this petition for a writ of certiorari should be granted.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that he has on this 23rd day of August, 1977, complied with the Supreme Court Rule 33 by mailing three (3) copies of this Petition to the following attorney:

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Bruce G. Murphy

Bruce G. Murphy, P.C.

UNPUBLISHED

United States Court of Appeals

FOR THE FOURTH CIRCUIT

No. 76-1418

Doris M. Bauer, Lou Ann
Murphy and Bruce G. Murphy,

Appellants,

versus

Thomas W. Gilliam, Jr.,
Erie Cocke, Jr., and
Madelyn Grotnes Cocke,

Appellees.

No. 76-1419

Doris M. Bauer, Lou Ann
Murphy and Bruce G. Murphy,

Appellees,

versus

Thomas W. Gilliam, Jr.,
Erie Cocke, Jr.,

Appellants,

and

Madelyn Grotnes Cocke,

Defendant.

Appeal from the United States District Court for the Eastern District of Virginia, at Norfolk. John A. MacKenzie, District Judge.

Submitted December 9, 1976 Decided February 22, 1977.

Before HAYNSWORTH, Chief Judge, WINTER and BUTZNER, Circuit Judges.

PER CURIAM:

The plaintiffs gave Frank E. Mower money to invest in wine franchises originating in Robert Dale Johnson's now infamous Ponzi scheme. Mower used the plaintiffs' money in addition to other funds to invest in the scheme through the defendants. The evidence indicates that neither the defendants nor Mower were aware of the fraudulent nature of the scheme. Both Mower and the defendants suffered huge financial losses when the scheme collapsed.

After the scheme collapsed, the plaintiffs brought this action against the defendants alleging numerous violations of federal and state securities laws, common law fraud and negligence, and there were other counts. The jury found for the defendants. The plaintiffs appealed to this court claiming that the trial court erred in denying their motion for a continuance and in instructing the jury.

The plaintiffs say that the denial of their request for a continuance prevented Stanley Sacks from representing them. According to the plaintiffs, Sacks' services were essential because Robert H. Bennett, who had been representing the plaintiffs, would violate the Code of Ethics if he served as counsel when his law partner, Bruce Murphy, was a plaintiff. There is no merit to this argument. The district court resolved all ethical conflicts in favor of Bennett and Murphy. The trial date had been set six

months in advance. Sacks could not have represented the plaintiffs in any event due to a conflict of interest which he discovered after he had agreed to represent them if the case were continued.

The plaintiffs assert that portions of the district court's instructions to the jury were erroneous and prejudicial. It is difficult to assess the merits of the plaintiffs' attack on the instructions because the record does not contain a full transcript of the trial. Rather than a full transcript, the plaintiffs have only provided a transcript of the portion of the trial containing the district court's instructions to the jury and the return of the jury's verdict.

But we need not reach the merits of the plaintiffs' attack on the district court's instructions because there is no evidence in the partial transcript that the plaintiffs objected to the charge after it was given, as required by Rule 51, Fed. R. Civ. P. Thus we find that the plaintiffs have waived all objections to the district court's instructions.

Since we reject the plaintiffs' arguments regarding the denial of the continuance and the jury instructions, there is no need to reach the plaintiffs' contention that the district court erred in releasing the defendants' property from the receivership which had been created in order to ensure satisfaction of any verdict against the defendants.

We dispense with oral argument and affirm the judgment below.

AFFIRMED.

UNITED STATES COURT OF APPEALS

FOR THE FOURTH CIRCUIT

No. 76-1418

FILED

MAY 25 1977

U. S. COURT OF APPEALS
FOURTH CIRCUIT

Doris M. Bauer, Lou Ann Murphy and Bruce G. Murphy,

Plaintiffs-Appellants,

versus

Thomas W. Gilliam, Jr., Erie Cocke, Jr. and Madelyn Grotnes Cocke,

Defendants-Appellees.

O R D E R

Upon consideration of the petition for rehearing filed by the plaintiffs-appellants,

With the concurrence of Judge Winter and Judge Butzner, it is ORDERED

That paragraph two of page 4 be stricken and the following paragraph be substituted in lieu thereof:

> Instructions must be evaluated in light of the evidence presented at trial. On the basis of the truncated transcript before us we cannot find that there was prejudicial error in the instructions here.

In all other respects the petition for rehearing is denied.

Chief Judge, Fourth Circuit

May 18, 1977

A True Copy, T e s t e:

William K. Slate, II, Clerk

By Faye L. Smith
Deputy Clerk